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TRUST RECEIPTS IN TEXAS

by

Arthur E. Sutherland* and Robert Braucher**

ON January 1, 1960, the Uniform Trust Receipts Act, enacted at the 1959 legislative session, took effect in Texas.¹ Thus, Texas became the thirty-seventh state, in addition to Puerto Rico, to enact the UTRA, promulgated in 1933 by the National Conference of Commissioners on Uniform State Laws.² In two of the thirty-seven states, Pennsylvania and Massachusetts, the UTRA has been superseded by the Uniform Commercial Code, also recommended by the Conference. The Code has also been enacted in four more states, Kentucky, New Hampshire, Connecticut, and Rhode Island, with postponed effective dates which have not yet arrived.^{2*} Connecticut and New Hampshire have the UTRA which will be superseded when the Code becomes effective. Professor Karl N. Llewellyn was the chief draftsman both of the UTRA and of the Code.

The provisions of the UTRA are intricate, and the Act is difficult to understand without knowledge of its historical background and of the relation of the trust receipt to other chattel security devices. Accordingly, we shall begin with a brief resume of the law of chattel security in Texas into which the trust receipt must fit, outline the history of the trust receipt, and describe the UTRA. We shall then be able to make some suggestions as to the probable impact of the UTRA in Texas, and to evaluate its enactment in the light of the availability of the Uniform Commercial Code as an alternative.

I. CHATTEL SECURITY

A. *Chattel Mortgages And The Statute Of Elizabeth*

For centuries the law has been troubled by the problems which arise when possession and property interests in things are separated; yet, innumerable human relationships make the separation inevitable. The lender of an automobile gives the borrower a fictitious air of

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¹ S.B. 237, approved May 30, 1959, Tex. Rev. Civ. Stat. Ann. art. 5499a-51 (Supp. 1959).

² See 9C Uniform Laws Ann. 59 (Supp. 1959).

^{2*} Pennsylvania, effective July 1, 1954; Massachusetts, effective October 1, 1958; Kentucky, effective July 1, 1960; New Hampshire, effective July 1, 1961; Connecticut,

prosperity, which conceivably may delude the borrower's creditors (a doubtful result in an economy where ownership of a car is more often a sign of unpaid debt than of substantial assets). A more difficult situation arises where the general owner remains in possession, but mortgages or otherwise encumbers his assets. For centuries he has been eyed suspiciously, as a probable cheat. In 1570, in the thirteenth year of Elizabeth's reign, the English Parliament enacted³

An act against fraudulent deeds, alienations, etc. . . .

intended to abolish the

feigned, covinous and fraudulent feoffments, gifts, grants, alienations, conveyances, bonds, suits, judgments and executions, as well of lands and tenements as of goods and chattels, more commonly used and practiced in these days than hath been seen or heard of heretofore: . . . not only to the let and hindrance of the due course and execution of law and justice, but also to the overthrow of all true and plain dealing, bargaining and chevisance between man and man, without the which no commonwealth or civil society can be maintained or continued: . . .

Like the classic naval designer's race between gun and armor, the law concerning encumbrances on chattels has long demonstrated a competition between the policy of this Statute of Elizabeth and the practical needs of the commercial community for the creation of security interests; a competition in which now one, now another, has prevailed. Reconciliation of these two inconsistent urges has ordinarily been made by a requirement of public recordation of the otherwise secret lien unless the secured party takes possession.⁴ This policy appeared early in the Texas statutes; from 1840 to the present time a chattel mortgage, if not recorded or filed in a public office, has been subordinate to the rights of creditors and subsequent purchasers.⁵

B. *Conditional Sales*

A mortgage is no less a mortgage because it secures the purchase price of the goods mortgaged; but at common law courts commonly

effective October 1, 1961; Rhode Island, effective January 2, 1962. See Braucher, *The Legislative History of the Uniform Commercial Code*, 58 Colum. L. Rev. 798 (1958); Malcolm, *The Uniform Commercial Code: Review, Assessment, Prospect-November, 1959*, 15 Bus. Law. 348 (1960). (Editor's Note. Since this Article was written, the Uniform Commercial Code has become effective in Kentucky.).

³ 13 Eliz. c. 5 (1570).

⁴ See Jones, *Chattel Mortgages and Conditional Sales* § 176 (6th ed. 1933); Gilmore & Axelrod, *Chattel Security*, 57 Yale L.J. 517, 761 (1948); Glenn, *The Chattel Mortgage as a Statutory Security*, 25 Va. L. Rev. 316 (1939).

⁵ Act February 5, 1840, §§ 4, 12, Laws of the Republic of Texas, 4th Cong. 153, as amended, Tex. Rev. Civ. Stat. Ann. art. 5490 (1958).

held a conditional sale, in which the seller retained title until the price was paid,⁶ to be a transaction quite distinct from a purchase-and-mortgage-back. In most states conditional sales were not subject to the chattel mortgage statutes. Early cases in Texas, however, seemed to adopt a contrary view identifying the conditional sale with the chattel mortgage.⁷ After the Supreme Court of Texas re-examined the question in 1885 and adopted the view usually followed in other states,⁸ the legislature declared conditional sales to be chattel mortgages, subject to the chattel mortgage requirements of writing and recordation.⁹ Texas soon held that conditional sales were subject to the same foreclosure procedure as well.¹⁰

Other states, during the period beginning in 1870, were also enacting statutes making conditional sales subject to rules similar to those governing chattel mortgages. In most states, however, the conditional-sale statute was separate, and different in minor respects, from the chattel mortgage statute. The Conference in preparing the Uniform Conditional Sales Act in 1917 rejected a suggestion that conditional sales simply be declared to be chattel mortgages.¹¹ Today it remains true that in most states the law governing the two security devices has not been harmonized, although the Uniform Commercial Code embodies a proposal to subject them to the same rules.¹²

C. Mortgages Of Inventory

One important distinction between chattel mortgages and conditional sales was retained in Texas after 1885. As in many other states,¹³ a chattel mortgage on a stock of goods exposed for sale in the usual course of the mortgagor's business was held in 1879 to be fraudulent and void as against creditors and purchasers even though recorded, and that decision was confirmed by statute the same year.¹⁴ Subse-

⁶ See Glenn, *The Conditional Sale at Common Law and as a Statutory Security*, 25 Va. L. Rev. 559 (1939).

⁷ *Knittel v. Cushing*, 57 Tex. 354 (1882); *Tufts v. Blanton*, 2 Will. § 294 (Tex. Comm. App. 1884); cf. *Key v. Braun*, 67 Tex. 300, 3 S.W. 443 (1887) (purchase-money mortgage).

⁸ *Leath v. Utley*, 66 Tex. 401, 17 S.W. 401 (1886); *City Nat'l Bank v. Tufts*, 63 Tex. 113 (1885); *Dunn v. Elser*, 2 Will. §§ 720-22 (Tex. Civ. App. 1885).

⁹ Acts 1885, at 76, now Tex. Rev. Civ. Stat. Ann. art. 5489 (1958).

¹⁰ *Harling v. Creech*, 88 Tex. 300, 31 S.W. 357 (1895).

¹¹ See *Burdick*, *Codifying the Law of Conditional Sales*, 18 Colum. L. Rev. 103, 107 (1918).

¹² Uniform Commercial Code § 9-102 (1958).

¹³ See *Cohen and Gerber*, *Mortgages of Merchandise*, 39 Colum. L. Rev. 1338 (1939).

¹⁴ *Peiser v. Pericolas*, 50 Tex. 638 (1879); Acts 1879, at 60, as amended, Tex. Rev. Civ. Stat. Ann. art. 4000 (Supp. 1959). The subsequent history of this rule in Texas is exhaustively discussed in *Williams*, *Security Interests in Goods, Fixtures and Equipment of Merchants and Manufacturers*, 25 Texas L. Rev. 589 (1947); *Comment*, 30 Texas L. Rev. 233 (1952).

quent decisions made it clear, however, that the rule of voidness of mortgages covering stocks of goods for sale did not apply to conditional sales of goods for resale, despite the 1885 statute assimilating conditional sales to chattel mortgages.¹⁵ It was not until 1949 that an amendment to the statute validated purchase-money mortgages on stocks of goods.¹⁶

A trace of the distinction, relating to buyers in ordinary course, may have survived the 1949 amendment. That amendment protects the retail buyer from the mortgagor "in good faith in the regular course of business." Previously such buyers had been protected, like other third parties, by the fact that the mortgage was fraudulent and void under the 1879 statute. Recorded conditional sales for resale, however, were not subject to that rule; and the protection of retail buyers from the conditional buyer had to be found in rules of agency and estoppel, if anywhere.¹⁷ Although there is recent dictum that it has "long been established" that the 1879 statute protects such a retail buyer,¹⁸ that statement seems to be erroneous; and there is no indication that the 1949 amendment extends the 1879 statute to conditional sales.

A further remnant of the distinction relates to the Texas Bulk Sales Law enacted in 1909.¹⁹ Before 1909 a valid security interest in inventory could be created by a deed of trust to the creditor, sales thereafter being made for the creditor's account.²⁰ But the Bulk Sales Law was held applicable to chattel mortgages on stock in trade,²¹

¹⁵ *Bowen v. Lansing Wagon Works*, 91 Tex. 385, 43 S.W. 872 (1898); *International Harvester Co. v. Smith*, 91 S.W.2d 827 (Tex. Civ. App. 1936) error dism.; *Park v. South Bend Chilled Plow Co.*, 199 S.W. 843 (Tex. Civ. App. 1917) error ref.

¹⁶ Acts 1949, c. 82, § 1, as amended, Tex. Rev. Civ. Stat. Ann. art. 4000 (Supp. 1959); *Pearson v. Rapstine*, 203 F.2d 313 (5th Cir. 1953). An exception for farm products had been added in 1935.

¹⁷ Cf. *Campbell Printing Press Co. v. Powell*, 78 Tex. 53, 14 S.W. 245 (1890); *Coleman Prod. Credit Ass'n v. Mahan*, 168 S.W.2d 903 (Tex. Civ. App. 1943); *Spadra Clarksville Coal Co. v. Security Nat'l Bank*, 206 S.W. 200, 201 (Tex. Civ. App. 1918); see *Williams*, *supra* note 14, at 598-99.

¹⁸ See *Donahue Inv. Co. v. H. E. McMasters Co.*, 301 S.W.2d 330, 331 (Tex. Civ. App. 1957) error ref. n.r.e. But see note 15 *supra*.

¹⁹ Acts 1909, at 66, as amended, Tex. Rev. Civ. Stat. Ann. art. 4001 (1945).

²⁰ *Bettes v. Weir Plow Co.*, 84 Tex. 543, 19 S.W. 705 (1892); see *Williams*, *supra* note 14, at 591. Unrestricted dominion in the debtor makes applicable the 1879 statute. *City Nat'l Bank v. Phillips*, 190 F.2d 97 (5th Cir. 1951).

²¹ *Universal Dealers Co. v. Vance*, 117 S.W.2d 512 (Tex. Civ. App. 1938) error dism.; *Beene v. National Liquor Co.*, 198 S.W. 596 (Tex. Civ. App. 1917); see *Larson*, *Bulk Sales: Texas Law and the Uniform Commercial Code*, 6 Sw. L.J. 417, 425 (1952). Foreclosure of a purchase-money mortgage was held not subject to the bulk sales law in *Southwestern Drug Corp. v. Webster*, 246 S.W.2d 241 (Tex. Civ. App. 1951).

although not to conditional sales.²² In most states transfers for security are not covered by the bulk sales laws.²³

D. Factor's Liens

In 1947 Texas became one of the many states to follow the lead of New York by establishing a statutory "factor's lien."²⁴ The statute allows a "factor," by written agreement, to create a lien on merchandise in the possession of the borrower, including after-acquired property. "Factor" is defined to include banks and others who advance money on the security of merchandise, whether or not they are employed to sell the merchandise. In effect the lien is a chattel mortgage on stock in trade and its proceeds. It is not limited to purchase money; indeed, retention of title by a seller seems not to be covered. When the merchandise is sold in the ordinary course of the borrower's business, the purchaser takes free of the lien, which attaches to the proceeds.

Elsewhere such statutes have been held to override the doctrine that a security interest is defeated if the borrower retains unrestricted dominion.²⁵ Section 10 of the Texas Act excludes "any stock of goods, wares or merchandise daily exposed to sale *at retail* in parcels in the regular course of business of such merchandise." (Emphasis added.) The quoted words, except those in italics, are identical with those in the 1879 statute;²⁶ and the effect seems to be to validate the lien for manufacturers, processors, wholesalers, and farmers, but not for retailers. Aside from the factor's lien statute, it is not clear whether the 1879 statute, which invalidates as against creditors and purchasers a mortgage on a stock of goods held for sale, applies to others than retailers.

The factor's lien requires a written agreement providing for the lien, and a written statement designating the merchandise signed by

²² Cf. *International Harvester Co. v. Smith*, 91 S.W.2d 827 (Tex. Civ. App. 1936) error dismissed; *Mayfield Co. v. Harlan & Harlan*, 184 S.W. 313 (Tex. Civ. App. 1916).

²³ See Uniform Commercial Code §§ 6-103(1), 9-111 (1958); Billig & Smith, *Bulk Sales Laws: Transactions Covered by These Statutes*, 39 W. Va. L. Rev. 323, 326-30 (1933). In cases involving mortgages of fixtures, federal district courts ruled that the Texas Bulk Sales Act did not apply to mortgages, disagreeing with *Beene v. National Liquor Co.*, 198 S.W. 596 (Tex. Civ. App. 1917). In *re Griffen Drug Co.*, 289 Fed. 140 (N.D. Tex. 1923); In *re Gary*, 281 Fed. 218 (S.D. Tex. 1922); In *re Martin*, 283 Fed. 833 (E.D. Tex. 1921). It is now clear that it does not apply to a transfer of fixtures except in conjunction with merchandise. *M Sys. Stores, Inc. v. Johnston*, 124 Tex. 238, 76 S.W.2d 503 (1934).

²⁴ Acts 1947, c. 180, as amended, Tex. Rev. Civ. Stat. Ann. art. 5506c (1958); see Skilton, *The Factor's Lien on Merchandise*, 1955 Wis. L. Rev. 356, 609; Comment, 37 Texas L. Rev. 456 (1959).

²⁵ *Colbath v. Mechanicks Nat'l Bank*, 96 N.H. 110, 70 A.2d 608 (1950); cf. Uniform Commercial Code § 9-205 (1958). See notes 14, 20 *supra*.

²⁶ Note 14 *supra*.

the borrower and delivered to the factor. In addition, a verified notice must be filed with the county clerk; the notice gives information about the parties and the duration of the agreement, but states only "the general character of the merchandise subject to the lien, or which may become subject thereto." There is no provision for filing the security agreement or a copy as in the case of chattel mortgages. A requirement that a sign be posted at the place where the borrower kept the goods was deleted by the amendment of the statute in 1955, following similar amendments in other states.

E. Accounts Receivable

As the factor's lien statute suggests, security interests in inventory commonly raise questions with respect to the proceeds received when the inventory is sold, and thus lead to consideration of the assignment of accounts receivable as security. The common law of Texas seems to have treated the assignment of a contract right as perfected when made, without any public record or notice to the obligor.²⁷ In 1945, in an apparently unnecessary effort to be sure that Texas assignments would be valid as against a trustee in bankruptcy,²⁸ the Texas legislature enacted a statute providing for the filing of a notice of assignment with the county clerk.²⁹

Two problems which have commonly arisen in other states in connection with assignments of accounts seem not to have been the subject of reported decisions in Texas courts before 1945. The first is the effect of a retention of unrestricted dominion by the assignor; the second is the effect of an assignment of rights under future contracts. The federal courts held that accounts were not subject to the 1879 statute on mortgages of goods daily exposed for sale,³⁰ but that an assignment could be invalidated by a separate principle

²⁷ *Employers' Cas. Co. v. Rockwall County*, 120 Tex. 441, 35 S.W.2d 690 (1931); *Hess & Skinner Eng'r Co. v. Turney*, 110 Tex. 148, 216 S.W. 621 (1919).

²⁸ *Corn Exch. Nat'l Bank v. Klauder*, 318 U.S. 434 (1943), held an assignment invalid in bankruptcy where notice required by state law had not been given. In *re Vardaman Shoe Co.*, 52 F. Supp. 562 (E.D. Mo. 1943), extended the rule to a non-notification state because of a possibility that an assignee might be estopped. *Contra*: In *re Rosen*, 157 F.2d 997 (3d Cir. 1946), cert. denied, *Fisch v. Standard Factors Corp.*, 330 U.S. 835 (1947). The problem was eliminated by amendment of the Bankruptcy Act in 1950. See *Assignments of Accounts Receivable*, 1946 Rep. N.Y. Law Rev. Comm. 351; *Conwill & Ellis, Much Ado about Nothing: The Real Effect of Amended 60 (a) on Accounts Receivable Financing*, 64 Harv. L. Rev. 62 (1950); *Craig, Accounts Receivable Financing: A Reappraisal of Validation Statutes in the Light of Amended 60 (a)*, 65 Harv. L. Rev. 627 (1952).

²⁹ Acts 1945, c. 293, amended by Acts 1955, c. 305, Tex. Rev. Civ. Stat. Ann. art. 260-1 (1959).

³⁰ *Coppard v. Martin*, 15 F.2d 743 (5th Cir. 1926), cert. denied, 273 U.S. 753 (1927).

against unrestricted dominion.³¹ The 1945 statute validating recorded assignments of accounts seems to recognize a rule against unrestricted dominion by section 8, providing that the return of merchandise sold does not impair the assignee's right to any balance remaining owing, even though the assignee acquiesces in the assignor's dominion over the returned merchandise.³² The only decision on this question under the statute is a 1951 federal case in which the court ruled that the assignor had not retained unrestricted dominion.³³

The same case seemed to assume that a filing under the statute protected assignments of after-acquired accounts during the three-year filing period.³⁴ Such an assumption was contrary to the statutory definition of "account" in terms of rights "under an existing contract," and the state courts held that the contract must be "existing" at the time the notice was filed.³⁵ The rule was changed by amendment of the statute in 1955, and filing now protects assignments of accounts arising out of "existing or future contracts" during the three-year period, "regardless of whether such account was in the contemplation of the assignor and assignee when such notice was executed."³⁶

F. Automobiles

A Texas statute enacted in 1933 gave effect to registered chattel mortgages on motor vehicles even though "daily exposed for sale," but protected bona fide purchasers in such cases.³⁷ Otherwise, automobiles remained subject to the chattel mortgage laws until 1939

³¹ *City Nat'l Bank v. Zorn*, 68 F.2d 566 (5th Cir. 1934).

³² Cf. *Manchester Nat'l Bank v. Roche*, 186 F.2d 827, 833 (1st Cir. 1951), interpreting a similar provision as to accounts receivable contained in the New Hampshire Factors Lien Act. Section 6 of the Texas Factor's Lien Act is similar. See note 24 *supra*.

³³ *Second Nat'l Bank v. Phillips*, 189 F.2d 115 (5th Cir. 1951), reversing *In re American Creameries Co.*, 90 F. Supp. 618 (S.D. Tex. 1950).

³⁴ See *In re Cumings*, 99 F. Supp. 690 (S.D. Tex. 1951), *rev'd*, *United States v. Phillips*, 198 F.2d 634 (5th Cir. 1952).

³⁵ *Keeran v. Salley*, 244 S.W.2d 663 (Tex. Civ. App. 1951) error ref.; Note, 31 Texas L. Rev. 63; followed, *Republic Nat'l Bank v. Vial*, 232 F.2d 785 (5th Cir. 1956). But cf. *Oklahoma Oxygen Co. v. Citizens State Bank & Trust Co.*, —Okla.—, 274 P.2d 372 (1954) (Texas law).

³⁶ Acts 1955, c. 305. That amendment and Acts 1957, c. 348, also dealt with assignments under construction contracts, and the priority of the surety on a payment or performance bond. See *National Sur. Corp. v. United States*, 132 Ct. Cl. 724, 133 F. Supp. 381, cert. denied, 350 U.S. 902 (1955); *R. F. Ball Constr. Co. v. Jacobs*, 140 F. Supp. 60 (W.D. Tex. 1956), *aff'd*, 239 F.2d 384, *rev'd*, 355 U.S. 587 (1958); *Tezel & Cotter v. Roark*, 301 S.W.2d 179 (Tex. Civ. App. 1957) error ref.; *Scarborough v. Victoria Bank & Trust Co.*, 250 S.W.2d 918 (Tex. Civ. App. 1952) error ref.

³⁷ Acts 1933, c. 117, Tex. Rev. Civ. Stat. Ann. art. 5497(a) (1958).

when the Texas Certificate of Title Law was enacted.³⁸ Under the Certificate of Title Law, security interests are now to be noted on the importer's or manufacturer's certificate or, after a retail sale, on the receipt or certificate of title issued by the Highway Department. The 1933 statute, the filing provisions governing chattel mortgages, and the statute invalidating mortgages on stock in trade are all superseded so far as they affect automobiles.³⁹

II. TRUST RECEIPTS BEFORE THE UTRA

A. *Origin*

The trust receipt seems to be a product of American legal ingenuity.⁴⁰ Banks on the eastern seaboard began to use it in the latter part of the nineteenth century in import transactions. A seller of a quantity of shellac ships the goods to a buyer in Boston who has agreed to pay for them on the presentation of a draft and a bill of lading. The Bombay seller wishes to keep control of the goods until assured of his money, and to accomplish this he sends his draft and bill of lading to a Boston bank with instructions to surrender the bill of lading only when the draft is paid. The Boston bank, pleased to arrange a loan with a Boston customer, pays the draft, and thus acquires a security interest in the bill of lading. The Boston buyer in many cases lacks the ready cash to pay the bank and pick up the bill; as a practical matter he has to get the goods off the ship, through the Custom House, and into the hands of a sub-purchaser. This *impasse* could have been solved, somewhat clumsily to be sure, if the buyer gave a properly recorded chattel mortgage on the goods to the bank. Instead, a device called the trust receipt was invented. The bank allowed the buyer to have possession of the bill of lading, and thus to gain possession of the goods upon the buyer's signing a receipt specifying the purposes of the arrangement and ordinarily agreeing to pay over the proceeds of the goods at once to the bank.⁴¹

Such transactions appealed to judges in the great commercial states as being economically desirable. Although unrecorded, the trust receipt was upheld as against subsequent encumbrancers. It escaped

³⁸ Acts 1939, at 602, as amended, Tex. Penal Code Ann. art. 1436-1 (Supp. 1959); see Couch, The Texas Certificate of Title Law, Tex. Penal Code, xiii (Commentary 1953); Wood, The Texas Certificate of Title Act, 5 Sw. L.J. 423 (1951); Woodward, The Constitutional Lien on Chattels in Texas, 28 Texas L. Rev. 305, 331-39 (1950).

³⁹ Bank of Atlanta v. Fretz, 148 Tex. 551, 226 S.W.2d 843 (1950); Motor Inv. Co. v. City of Hamlin, 142 Tex. 486, 179 S.W.2d 278 (1944); Commercial Credit Co. v. American Mfg. Co., 155 S.W.2d 834 (Tex. Civ. App. 1941) error ref.

⁴⁰ See McGowan, Trust Receipts (1947).

⁴¹ The facts are substantially those of *Moors v. Kidder*, 106 N.Y. 32 (1887). An earlier case is *Barry v. Boninger*, 46 Md. 59 (1877).

the statutes requiring recordation of chattel mortgages and conditional sales on the theory that a trust-receipt transaction was neither. The reasoning was highly technical. Courts said the transaction was not a chattel mortgage because the title was not in the buyer, and it was not a conditional sale because the bank was not selling to the buyer. Through this narrow gap the trust receipt was carried to success in a number of states. The device was a useful one, and soon spread from foreign trade to domestic business, including the immense trade in automobiles.⁴²

B. *Texas Decisions*

The first Texas case dealing with a trust receipt under that name seems to have arisen in 1925.⁴³ It involved the classic three-party pattern of seller, buyer, and lender. The buyer was a retail dealer in automobiles; the lender paid the purchase price of a stock of cars, securing himself by taking a trust receipt covering the cars. The court of civil appeals held the trust receipt "absolutely void," at least as against the automobile dealer's trustee in bankruptcy and other third parties: it was a chattel mortgage on a stock of merchandise daily exposed for sale in parcels at retail, and void under the 1879 statute; or, if it was a "reservation of title," it was void because not recorded. A similar ruling the following year, involving what appears to have been a two-party transaction—essentially a conditional sale—was refused review by the Texas Supreme Court; in that case, moreover, the taking of possession by the entruster was ineffective under the Bulk Sales Act.⁴⁴

Later, however, the commission of appeals upheld a three-party trust receipt on automobiles.⁴⁵ The 1879 statute was held inapplicable because there was a reservation of title rather than a conveyance by an owner.⁴⁶ Although the transaction should have been recorded as a chattel mortgage, the competing mortgagee had received actual notice and could not take advantage of the failure to record. That decision seems to have settled the law both as to the effect of exposure to sale and as to the requirement of recording.⁴⁷ Although repossession by an entruster under unrecorded trust receipts did not

⁴² See *In re James, Inc.*, 30 F.2d 555 (2d Cir. 1929).

⁴³ *GMAC v. Boddeker*, 274 S.W. 1016 (Tex. Civ. App. 1925).

⁴⁴ *Texas Bank & Trust Co. v. Teich*, 283 S.W. 552 (Tex. Civ. App. 1926) error ref.

⁴⁵ *Commercial Credit Co. v. Schlegel-Storseth Motor Co.*, 23 S.W.2d 702 (Tex. Comm. App. 1930).

⁴⁶ See note 15 *supra*.

⁴⁷ *Tyler State Bank & Trust Co. v. Bullington*, 179 F.2d 755 (5th Cir. 1950); *C.I.T. Corp. v. Haynie*, 135 S.W.2d 618 (Tex. Civ. App. 1939).

violate the Texas Bulk Sales Act,⁴⁸ it could constitute a voidable preference under Section 60 of the Bankruptcy Act.⁴⁹

C. The Need For The UTRA

In many states the trust receipt was upheld as being neither a chattel mortgage nor a conditional sale, so long as it adhered to the three-party pattern. But as requirements of public record became more common for both conditional sales and chattel mortgages, complete exemption from any such requirement began to seem more and more anomalous, and by 1930 the trend of the decisions, as in Texas, was to hold that the trust receipt was subject to recording either as a conditional sale or as a chattel mortgage.⁵⁰ Moreover, the recording statutes commonly contained requirements that individual transactions be separately recorded and that the collateral be described with some particularity; those requirements seemed inconvenient if not impracticable in many lines of trade when applied to stocks of goods.

To meet the problem, Professor Llewellyn drew up the Uniform Trust Receipts Act, and the Conference promulgated it in 1933. Its essentials are a simplified filing provision, a validation of the security interest as against the creditors of the "trustee," and the protection of the "buyer in the ordinary course of trade" from the trustee. Ten states adopted the UTRA in the 1930's, 16 in the 1940's, and 11 in the 1950's; Texas is the latest.⁵¹

III. THE UNIFORM TRUST RECEIPTS ACT

Summary paraphrase of any statute is a hazardous venture, and the risk increases directly with the complexity of the statute's verbiage. The Trust Receipts Act is highly technical. Its sections are involved and interrelated. One undertakes an abridgement with hesitation, and with a consciousness that in the process many refinements, many qualifications, must be elided. They will be evident only to the resolute reader who attacks the Act itself. But such a summary as appears here may show the main thrust of the statute, and perhaps will ease the labor of one who first faces the text of the Act itself.

A. The "Trust Receipt Transaction": Section 2

In considering the theory on which the Trust Receipts Act was

⁴⁸ See note 22 *supra*.

⁴⁹ *Tyler State Bank & Trust Co. v. Bullington*, 179 F.2d 755 (5th Cir. 1950).

⁵⁰ E.g., *GMAC v. Berry*, 86 N.H. 280, 167 Atl. 553 (1933).

⁵¹ See note 2 *supra*.

drafted in 1933, one has to keep in mind what was, at that time, the comparatively startling nature of a proposal to validate a mortgage on a shifting stock of goods and on the proceeds of its current sales, despite the mortgagor's dominion over the goods and the proceeds. The draftsman thought it necessary to restrict the operation of the statute to something resembling the classic trust receipt transaction. To accomplish this restriction, section 2 of the Act defines a "trust receipt transaction" both by prescribing the procedure for the creation of the security interest and by prescribing its purpose. A "trust receipt transaction," as so defined, may cover goods, documents of title to goods, or (as an extension of the classic trust receipt transaction) it may cover "instruments" which, under the definition of section 1 of the Act, may include ordinary negotiable instruments, certificates of stock, bonds, debentures, or other investment paper. The precise routine of the old tripartite deal is not required. The essential is that the entruster take from the trustee a writing indicating that a security interest is created or affirmed. The extension of the definition of the trust receipt transaction to cover certain transfers of negotiable paper and other investment securities was made in recognition of a widespread practice of stockbrokers and of the bankers who finance them.

To come within the protection of the statute, the transaction must be for one of three purposes. First, in the case of goods, documents, or instruments, the transaction may be for their sale or exchange. Secondly, in the case of goods or documents, the transaction may be for manufacture or processing of the goods in question with the purpose of ultimate sale; or for some operation connected with shipment or storage preliminary to sale. Finally, in the case of "instruments" the transaction may be for the purpose of delivering them to a principal under whom the trustee holds them as agent; or it may be for some transaction involving delivery to a depositary or registrar; or for presentation, collection, or renewal.

As a further precautionary limitation, section 15 of the Act denies its application to "single transactions of legal or equitable pledge, not constituting a course of business" and provides that the Act does not apply to transactions of bailment or consignment where the bailor or consignor does not retain title for security of an indebtedness due to him.

B. Recordation: Section 13

The provision for recordation devised in 1933 was novel and ingenious. It has since been adopted in other legislation, notably in

article 9 of the Uniform Commercial Code. Under section 13 of the UTRA a prospective "entruster" files in a public office a short "Statement of Trust Receipt Financing" which refers interested persons to the entruster for detailed inquiry about outstanding trust receipt transactions. The entruster recites that he is or expects to be engaged in financing under trust receipt transactions the acquisition by the trustee of goods of a certain sort described in general terms such as "coffee, silk, automobiles, or the like." The entruster and the "trustee" (who scarcely resembles a trustee in the usual sense) must both sign the statement. There is no provision for public recordation with respect to transactions in "instruments."

Public filing of this one short paper will serve for a very large number of transactions. For each transaction the trustee simply gives to the entruster a trust receipt which designates the goods or documents concerned and recites that a security interest will accrue to the entruster. Public filing of a large number of separate papers is thus eliminated.

C. Validity Against Creditors: Section 8

Section 8 of the Act provides that the entruster's security interest is good without filing as against all creditors, with or without notice, for thirty days after delivery of the goods, documents, or instruments to the trustee. Texas has enacted this thirty-day provision despite the conflicting and prevailing provision of section 60 A(7)I of the Bankruptcy Act,⁵² which permits such a lien to be valid as against a trustee in bankruptcy for not more than twenty-one days. The draftsmen of the Uniform Commercial Code, section 9-304(5), have wisely restricted their corresponding provision to a twenty-one day period which conforms to the Bankruptcy Act.

A lien creditor who gets his lien after the period is over, without notice of the trust receipt interest, and before filing, prevails over the entruster. Section 8(3) of the Act makes a trustee in bankruptcy an assignee for creditors or an equity receiver the equivalent of a lien creditor without notice for the benefit of all creditors, lien or otherwise, unless all creditors have had notice of the entruster's security interest, or filing has occurred, or the entruster has taken possession.

The Bankruptcy Act, section 70 C,⁵³ makes slightly different provisions; it gives the trustee in bankruptcy the rights of a lien creditor "whether or not such a creditor actually exists." The Uniform

⁵² 52 Stat. 869 (1938), 11 U.S.C.A. § 96 (1943).

⁵³ 66 Stat. 429 (1952), 11 U.S.C.A. § 110 (1953).

Commercial Code, section 9-301(3), resembles the provisions of the Trust Receipts Act in this respect.

D. Protection Against Purchasers: Section 9

Section 9 of the Act protects those who in good faith and for value purchase from the trustee negotiable instruments or documents or "instruments in such form as are by common practice purchased and sold as if negotiable." Filing does not give notice to purchasers of such paper except in the case of "transferees in bulk." Other purchasers from the trustee are protected even if filing has occurred, provided they are buyers in the ordinary course of trade. Purchasers other than buyers in ordinary course who obtain delivery of goods before filing, and who in good faith and without notice either give "new value" before the expiration of the "thirty day period" or who give "value" after that period hold the subject matter free from the entruster's security interest. As defined in section 1 of the Act, "value" means any consideration sufficient to support a simple contract, including an antecedent debt; "new value" includes new advances, or loans made or new obligations incurred or the release of an existing security interest. Extensions or renewals of existing obligations of the trustee are not "new value," nor are obligations substituted for such existing obligations. In all cases covered by section 9, credit extended by the seller is "new value."

E. Entruster's Right To Proceeds: Section 10

Section 10 of the Uniform Act gives to the entruster in specified circumstances a lien on the proceeds of the goods, documents, or instruments when disposed of by the trustee. For this lien to arise, however, the trustee must have undertaken to account for proceeds. Where the proceeds are not identifiable, the Act, nevertheless, purports to give a limited right to their value and to give a priority in insolvency, thus raising still another question of conflict with the Bankruptcy Act.⁵⁴

F. The Abortive Trust Receipt: Section 3

In the course of business life there are many instances of "pledge" or attempted pledge without delivery of possession to the secured creditor. In view of the Act's complex definition of a trust receipt

⁵⁴ In re Harpeth Motors, Inc., 135 F. Supp. 863 (M.D. Tenn. 1955). Contra: In re Crosstown Motors, Inc., 272 F.2d 224 (7th Cir. 1959). Cf. Uniform Commercial Code § 9-306(4).

transaction in section 2, a certain number of such attempted transactions may fall short of compliance. Section 3 gives for a period of ten days a limited protection to "an attempted pledge or agreement to pledge not accompanied by delivery of possession which does not fulfill the requirements of a trust receipt transaction" As against creditors of the pledgor, such an attempt will create a valid interest only to the extent that the pledgee gives "new value" in reliance on the pledge; it will be valid in that case as against all creditors with or without notice for ten days from the giving of new value. A lien creditor without notice who becomes such before the pledgee takes possession will prevail over the pledgee where the pledge is not for "new value," and such a creditor will prevail even in the case of new value after the lapse of ten days.⁵⁵

G. General Commentary On The Act

The Trust Receipts Act provides a convenient mechanism for securing indebtedness, in carefully limited situations, by a lien which may cover a stock of goods held for resale, and which may cover the proceeds of that stock when sold. Rights of lien creditors and other creditors represented by trustees in bankruptcy and similar functionaries under federal or state law are carefully defined, and the position of the buyer in ordinary course is made clear. The Act provides a cheap and convenient means of public record of the intention of the parties to create a series of trust receipt transactions. With the increasing acceptance of the idea that a mortgage on a floating stock of goods and its proceeds is a normal and proper type of transaction, one wonders whether the Trust Receipts Act today needs such a complicated and restrictive definition of a "trust receipt transaction." Would not the Act be more useful and less puzzling if it were so drawn as to apply more broadly?

IV. APPRAISAL

Whoever drives the same automobile for many years comes to the sad moment of realization that no amount of further repairs of a rachitic motor, fuming radiator, or groaning transmission will produce a reliable machine. Despite the easy familiarity of the old family vehicle, the time has come when one should buy a new car. The same phenomenon, *mutatis mutandis*, occurs in statutory reform of the law. Spot repairs to take care of comparatively restricted needs

⁵⁵ See the Note entitled "What the Uniform Trust Receipt Act Does", 9C Uniform Laws Ann. 223-29.

can be made here and there, but every now and then general coordinated fresh revision of a large area of the law is a better step.

In Texas as in many other states the mortgage of personal property appears in many statutory guises. The old familiar chattel mortgage is described in one statute; conditional sales appear in another. In 1945 the Texas Legislature made provision, perhaps then unnecessary, to validate assignments of accounts. "Factor's liens" were covered by a new statute in 1947. Purchase money mortgages on stocks of goods were validated in 1949. On January 1, 1960, the Trust Receipts Act appeared in the galaxy.

The difficulty with such piecemeal legislation is the possibility of unintended gaps or inconsistencies in the law. The parts do not necessarily fit together. Statutes intended to fulfill a specific purpose may be drafted by those particularly concerned, without an overall survey of the scene. The special merit of the Uniform Commercial Code is its inclusive view, as clearly appears from a Staff Research Report on the Code and a Monograph Analysis of Article 9 made by the Texas Legislative Council in 1955 and 1954 respectively.⁵⁶ Even in the limited area covered by the Trust Receipts Act, the Commercial Code has eliminated some troubles.⁵⁷ The Trust Receipts Act was a forerunner of the Code in four states. Perhaps Texas will see the wisdom of their example.

⁵⁶ Staff Research Report: "Analyses of the Uniform Commercial Code", Texas Legislative Council, August 1955. Staff Monograph: "Analyses of Article 9 of the Uniform Commercial Code", Texas Legislative Council, May 1954.

⁵⁷ Kripke, *The Modernization of Concepts Under Article 9 of the Uniform Commercial Code*, 15 *Bus. Law.* 645, 648 (1960).